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ABSTRACT

This paper reviews the trade policy situation in the Central African Republic (CAR) and identifies a number of key issues and challenges for the country. The focus of the study is thereby on how trade taxes and quantitative restrictions affect the goods sector. The analysis falls into three parts. First, the state of domestic trade policy is described, with particular emphasis on the structure and economic effects of border policies. Then, CAR's regional integration efforts are examined, including a preliminary assessment of the impacts of the formation of the CEMAC customs union. And finally, some priorities for the attention of policy makers and international donors are identified based on the preceding analysis.

KEYWORDS

Trade, tariffs, border taxes, regional integration, Economic Partnership Agreement

JEL CLASSIFICATION

F13; F14; F15; O24

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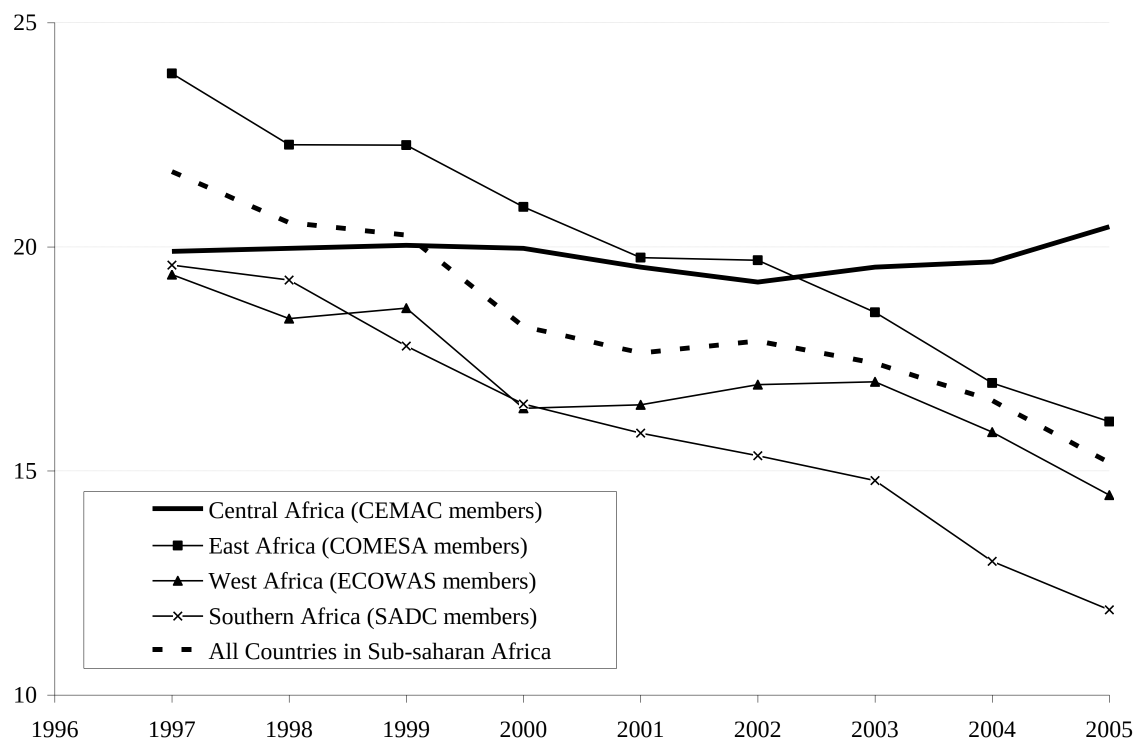
TRADE POLICY AND REGIONALISM IN THE CENTRAL AFRICAN REPUBLIC *

1. BACKGROUND

Over the past decade, countries in Sub-Saharan Africa have, in general, made significant progress in opening up their economies to international markets by reducing duties on imports. Between 1996 and 2005, the average tariff in the 47 countries south of the Sahara fell from 22 per cent to 15 per cent. This trend towards greater liberalization of domestic markets was observable throughout West, East, and Southern Africa, but not in Central Africa. Indeed, the tariff average in member states of the Economic and Monetary Community of Central Africa (CEMAC) remained flat for most of the past decade and even increased slightly in recent years (Figure 1). Central Africa thereby turned from a relatively low protection region by African standards to a high protection region. Tariff protection in CAR, which is a member of CEMAC, closely follows the trend in other Central African countries.

Figure 1: Tariff averages in sub-Saharan Africa
(in per cent)



Note: Averages based on simple mean of applied tariffs (i.e. most favored nation (MFN) duties plus customs surcharges). Regional averages are calculated based on membership in the respective regional trade agreements as of July 2006. The membership in the Common Market of Eastern and Southern Africa (COMESA) and the Southern African Development Community (SADC) overlaps.
Source: World Bank staff.

* This background paper for the CAR-Diagnostic Trade Integration Study was prepared in August 2006 by Peter Walkenhorst, Senior Economist, International Trade Department, World Bank, Washington DC.

The following discussion reviews the trade policy situation in CAR and identifies a number of key issues and challenges for the country. The focus of the study is thereby on how trade taxes and quantitative restrictions affect the goods sector. The analysis falls into three parts. First, the state of domestic trade policy is described, with particular emphasis on the structure and economic effects of border policies. Then, CAR's regional integration efforts are examined, including a preliminary assessment of the impacts of the formation of the CEMAC customs union. And finally, some priorities for the attention of policy makers and international donors are identified based on the preceding analysis.

2. DOMESTIC TRADE POLICIES

2.1 Border Policies

CAR is a member of the World Trade Organization (WTO) since May 1995 and its trade policy is guided by adherence to WTO rights and obligations. CAR applies the common external tariff of the Community of Central African Countries (CEMAC) and grants at least most-favored-nation (MFN) treatment to its trading partners. CAR has tariff bindings at rates ranging from 20 per cent to 70 per cent on goods in 3 529 tariff lines (at the Harmonized System (HS) 8-digit level), i.e. in 62.5 per cent of all tariff lines. The average bound tariff amounts to 36 per cent. Tariff bindings represent the maximum allowable tariffs that WTO members have scheduled as part of their commitments in multilateral trade negotiations. Application of import duties above bound rates is not allowed, unless trading partners adversely affected by the tariff change are compensated.

Yet, countries are free to apply import duties that are lower than their bindings, which is the case in CAR. The country's simple MFN-tariff average across all tariff lines (at the HS 10-digit level) was 19.1 per cent in 2005, and the import-weighted average amounted to 17.1 per cent (Table 1). The applied tariff structure employs five duty bands, ranging from zero to 30 per cent. Medical equipment and supplies and educational materials can enter the country free of import duty, while tariffs of 5, 10, 20, and 30 per cent, respectively, are charged on essential goods, raw materials and capital goods, intermediate goods, and consumer goods. Of the 6 172 tariff lines, 6 095 (or 99 per cent) are non-zero, with 2 471 (40 per cent) being subject to the highest duty rate of 30 per cent.

In addition to the MFN-tariffs, CAR applies a 10 per cent anti-pollution tax on imports of used cars, and a variable levy on petroleum imports. The amount of the latter is linked to the difference between the regulated domestic petroleum price and the import price. As the domestic petroleum price has not been changed since 2000, the increase in world petroleum prices since then has meant that the petroleum levy has been declining over time. Indeed, at petroleum prices of more than USD 70, the petrol tax has become negative, i.e. turned into an import subsidy.

Imports from other members of CEMAC enter CAR in principle under preferential conditions. In particular, CAR practices regional free trade, so that imports from CEMAC countries can enter the Central African market without paying duty. However, since May 2004 the country applies a derogation to the Community's free trade arrangement that allows it to treat imports of selected products from CEMAC partners as originating outside the Community and levy a Community Preference Duty ("Taxe de Préférence Communautaire"), which is equal to the MFN duty, on them. The products concerned include prepared foods, wine, whisky, and cosmetics. The derogation was originally designed to temporarily protect CAR against import surges over a period of six months, but has subsequently been renewed several times.

Table 1: Characteristics of the import regime in the Central African Republic, 2005

Product classification (SITC-3)	Structure of MFN tariffs: Number of tariff lines	Min. tariff (%)	Max. tariff (%)	Avg. MFN (%): Simple tariff avg	Import w'ted avg.	Import value: Million FCFA	Per cent
Food & live animals	731	0	30	24.7	26.3	12 504	19.6
Beverages & tobacco	46	10	30	27.4	17.1	2 254	3.5
Crude materials, except food & fuel	740	0	30	20.9	25.4	2 240	3.5
Mineral fuel & lubricants	58	10	20	10.2	10.0	13 642	21.4
Animal & veg oils, fats & wax	48	10	30	24.8	30.0	1 064	1.7
Chemicals & related products	909	0	30	11.0	7.0	6 736	10.6
Manufactured goods	1 720	0	30	20.2	19.1	9 353	14.7
Machinery & transport equipment	1 058	0	30	14.4	16.4	12 364	19.4
Miscellaneous manufatured articles	850	0	30	24.8	19.4	3 539	5.6
Other commodities	12	0	30	15.0	-	0	0.0
Total	**6 172**	**0**	**30**	**19.1**	**17.1**	**63 697**	**100.0**

Note: All reported information is derived from data at the tariff line (HS 10-digit) level. Information on import value based on transactions processed through ASYCUDA, so that trade through non-computerized border stations, which is estimated at about 10 per cent of the total, is not covered.

Source: World Bank staff based on information from National Authorities.

Imports are also subject to several earmarked duties. In particular, CAR charges the CEMAC Community Levy ("Taxe Communautaire d'Intégration") of 1 per cent and the CEEAC Community Levy ("Contribution Communautaire d'Intégration") of 0.4 per cent on imports from countries outside CEMAC and CEEAC. Moreover, imports are subject to a 0.5 per cent information technology surcharge ("Redevance pour l'Equipement Informatique des Finances"), a 0.25 per cent road use charge ("Redevance d'Usage Routier"), and a 0.05 per cent surcharge to finance the operations of OHADA ("L'Organisation pour l'Harmonisation en Afrique du Droit des Affaires").

In addition, several non-trade specific taxes are collected at the border. In particular, importers have to pay a Presumptive Income Tax ("Impôt Minimum Forfaitaire") of 1 per cent for enterprises and 3 per cent for individuals. Moreover, excise taxes of 25 per cent apply to selected products, notably alcoholic beverages and tobacco, in 121 tariff lines. Imports are also subject to value-added tax (VAT), which was increased from 18 per cent to 19 per cent in January 2006 and applies to the customs value plus tariffs and excise duties. There are exemptions from VAT for essential products, which CAR implements in accordance with a corresponding CEMAC list of products in 224 tariff lines.

In sum, the total tax burden on imports can be very heavy and almost double the price of imported goods. In the extreme, a 30 per cent tariff plus 25 per cent excise tax multiplied by a VAT of 19 per cent to which earmarked duties of 2.2 per cent and a Presumptive Income Tax of up to 3 per cent are added brings the total tax levied on imports to 90 per cent. Such high levels of taxation provide a strong incentive for importers to search for possibilities of tax avoidance, including through undervaluation of merchandise and other illicit means.

Exemptions from import duties and other border taxes reduce the average burden on importers. Comparing government revenues from import duties with the value of imports makes it possible to determine the *ex-post* average tariff rate, which takes into account the reduced duties on imports under preferential agreements, duty exemptions, and "leakage" due to weak customs control. If the average of the import duty revenues for 2005 is related to the value of imports during that year, the *ex-post* average tariff rate comes to 8.9 per cent. Hence, the effectively paid tariff is only half as high as the trade-weighted average of listed rates. The corresponding average total *ex-post* burden of trade taxes on imports, including value-added, excise taxes, petrol taxes and customs surcharges, amounted to 26.9 per cent.

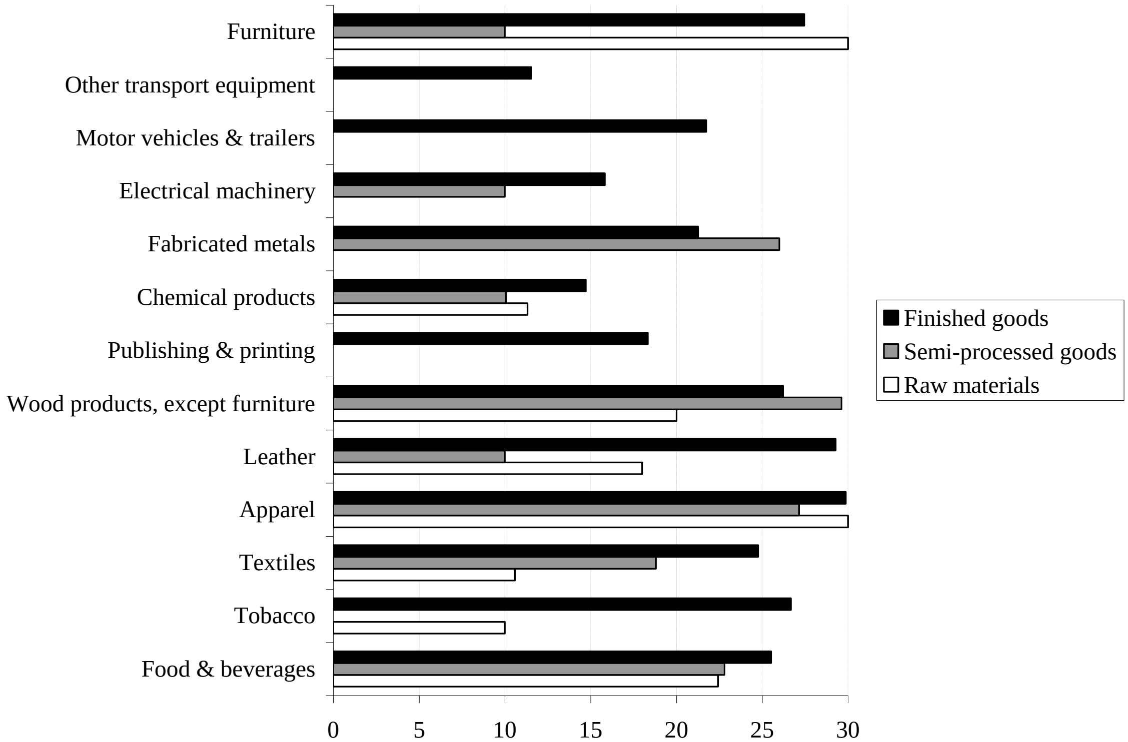
Import duties raise revenue to finance the functioning of the public sector, but the Government views import taxes also as a means of protecting domestic industry from foreign competition. CAR's tariff regime is generally escalatory, so that tariffs on finished goods are higher than tariffs on semi-processed products, which in turn are higher than tariffs on raw materials (Figure 2). While tariff escalation is a feature of trade policy in many countries, officials should be aware of the economic consequences and risks that such tariff structures bear for international competitiveness.

In particular, CAR's tobacco industry, which is a major industrial activity and accounts for almost 30 per cent of the country's total manufacturing value-added, turns out to be the sector with the highest degree of tariff escalation. Average tariffs on finished products are nearly 2.7 times as high as import duties on raw materials. This tariff protection gives rise to very high rates of effective protection and introduces a strong anti-export bias. Tobacco produced for the export market does not receive the same market price support that tobacco products for the domestic market enjoy, thus biasing producers' decisions against selling abroad. But companies that shy away from foreign markets tend to become less competitive over time and less capable of exploiting opportunities that might present themselves abroad. Hence, the very high effective protection granted to tobacco producers in CAR does not only hurt tobacco consumers by pushing up domestic prices, but also undermines the longer-term viability of tobacco manufacturing as a potential export sector.

Another sector that deserves the Government's attention is sugar production. Since November 2003, CAR has been operating an import quota regime for sugar. The quantitative restrictions have been put into place by invoking WTO safeguard provisions and are scheduled to remain in force until 2008. The policy is intended to facilitate the restructuring and modernization of the domestic sugar cane processing facility (Société de Gestion Sucrière en République Centrafricaine, SOGESCA) under its new, private owner (Sucrière en Afrique, SUCAF-RCA). The Government currently prohibits the establishment of a second sugar producer in the country, buys the annual output of the domestic cane processor of about 8 000 tons at regulated prices, and grants import licenses for about 15 000 tons of sugar to meet domestic demand. Under a memorandum of understanding, 90 per cent of the import licenses are allocated to SUCAF, so that this firm holds a near monopoly in the sugar market. It is reported that the company makes a bigger profit from resales of imported sugar than from its core cane processing activity. Domestic retail prices of about FCFA 750 per kilogram were nearly four times unit import prices (about FCFA 190 per kilogram) in 2005, which, even after application of import duties and value-added taxes, leaves a generous marketing margin. At the same time, the hoped-for technological upgrading and modernization of the domestic cane processing facility has been slow and domestic sugar production has not approached the envisaged level of 15 000 tons per year. In this context, the Government should review the effectiveness of its sugar policy with a view to abolish the quantitative import restrictions and liberalize imports.

Figure 2: Import duties by processing stage

(in per cent)



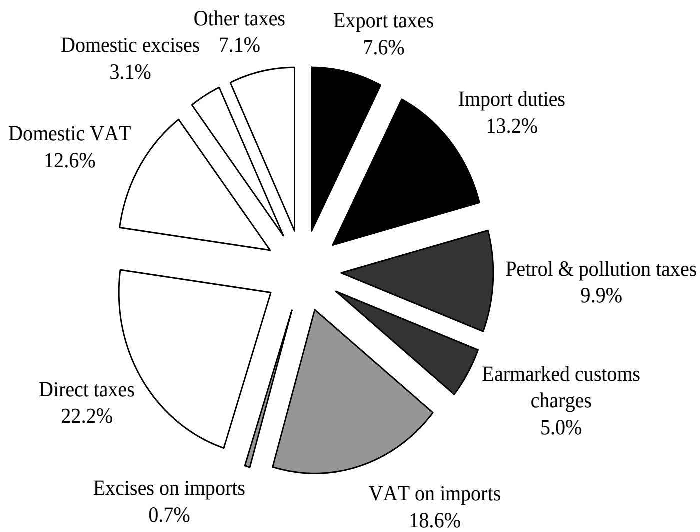
Note: Average of MFN duties at the tariff line (HS 10-digit) level.
Source: World Bank staff based on information from National Authorities.

Concerning exports, CAR applies export taxes (“droits de sorties”) to diamonds (4 per cent), gold (1 per cent), and timber (10.5 per cent on wood in the rough, 4.05 per cent on sawn wood). There used to be similar taxes on exports of coffee (8.15 per cent) and cotton (6.08 per cent), but these charges have been suspended since 1999 in order to alleviate the fiscal burden on the already struggling coffee and cotton producers. In addition to the export taxes, diamonds and gold exports are subject to a mining promotion charge (“taxe de promotion minière”), respectively, of 1 per cent and 0.75 per cent, and diamond and timber exporters have to pay an information technology surcharge of 0.5 per cent. Moreover, diamond exporters are liable to a 0.5 per cent charge for Kimberley process certification. Diamond, gold, and timber exporters also have to pay the Presumptive Income Tax at rates of, respectively, 3 per cent, 1 per cent, and 2 per cent.

2.2 Revenues from Trade Taxes

CAR continues to rely heavily on trade taxes to finance the government budget. In 2006, 55 per cent of all tax revenues are expected to relate to cross-border transactions (Figure 3). Trade-specific taxes, such as export taxes, import duties, petrol taxes, and customs charges, thereby account for two-thirds of trade tax revenue, while the remaining third is derived from general taxes collected at the border, such as VAT and excises.

Figure 3: Budgeted composition of Government revenues, 2006

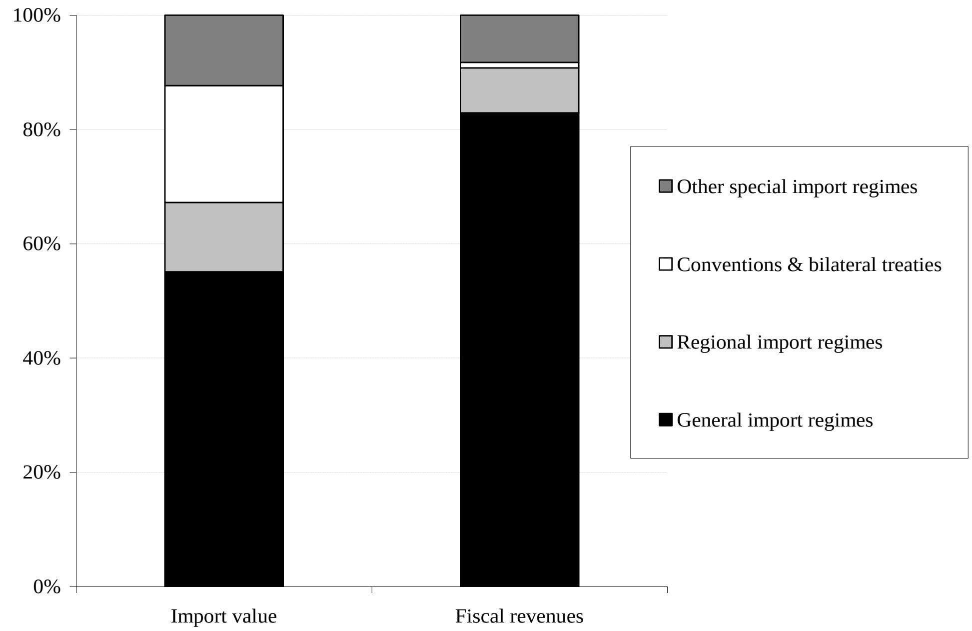


Source: République Centrafricaine, Loi de Finance, 2006.

The overwhelming share of trade taxes is collected on imports. In 2005, about 55 per cent of all incoming shipments entered CAR under the general customs regime, but these imports accounted for 83 per cent of all import tax revenues. In contrast, special trade regimes that offered exemptions under regional trade agreements, conventions and bilateral treaties, or other special arrangements provided merely 17 per cent of revenues, although they accounted for 45 per cent of imports (Figure 4). Hence, the existing exemptions led to a considerable loss of fiscal revenue. Indeed, if all imports under special regimes would have generated the same fiscal yield as the average of imports under the general customs regime (i.e. 40.5 per cent), import tax receipts would have been 50 per cent higher. Alternatively, without exemptions, the same revenue could have been raised with border taxes that are a third lower than those actually in effect.

These static calculations of lost revenue due to exemptions do not take the incentive effects of border taxes on trade flows into account. Any attempt to raise revenue through higher taxation of imports will tend to reduce import levels by discouraging shipments or diverting trade towards informal channels. CAR's heavy reliance on trade taxes for public finance purposes currently already provides little scope for trade policy to foster international integration and act as an engine of structural change and economic growth. In this context, the Government should resist temptations to continue raising taxes on trade, and instead look for opportunities to reduce the burden that is placed on importers and exporters.

Figure 4: Imports and fiscal revenues by customs regime, 2005



Note: Information based on transactions processed through ASYCUDA, so that trade through non-computerized border stations, which is estimated at about 10 per cent of the total, is not covered.
Source: World Bank staff based on information from National Authorities.

3. REGIONAL INTEGRATION

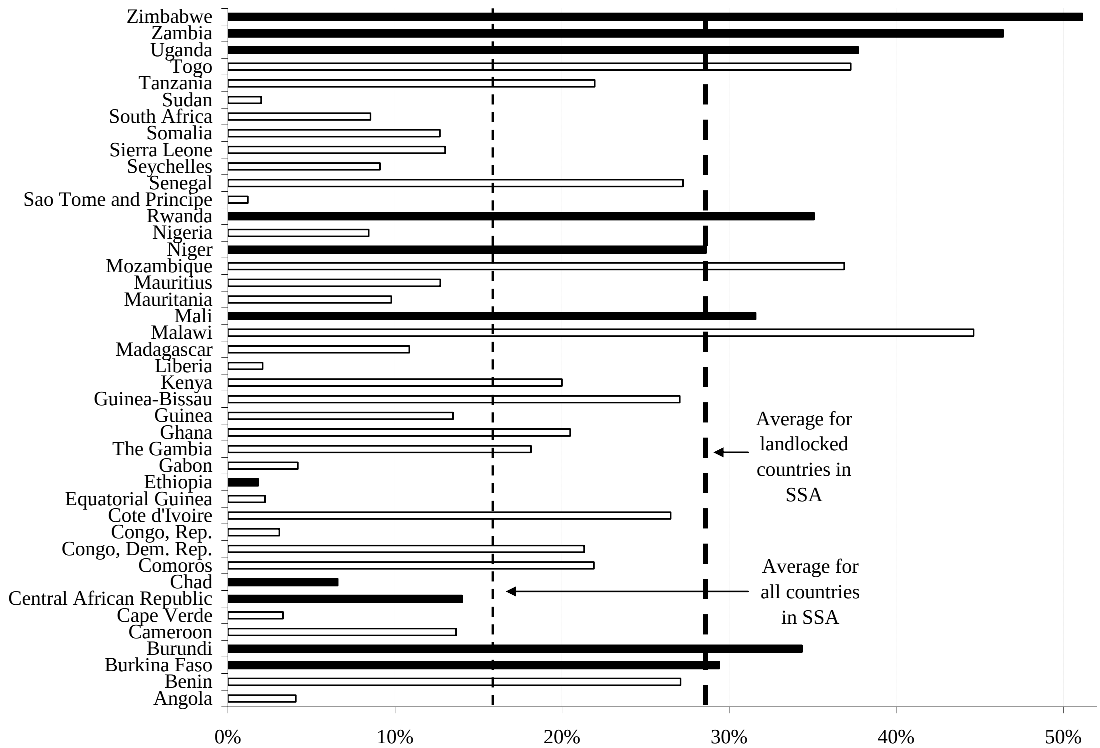
Like other countries in Central Africa, CAR is committed to the process of regional integration and is pursuing closer ties with neighboring nations. CAR is currently engaged in two regional trade agreements, namely the Community of Central African Countries (CEMAC) and, the Economic Community of Central African States (CEEAC). Moreover, CAR is a member of the Community of Sahel-Saharan States (CEN-SAD) and is party to several bilateral agreements, which are mainly focused on forms of regional integration other than trade.

Additional impetus for regional integration comes from the Economic Partnership Agreement (EPA) negotiations with the European Union. The Cotonou Agreement signed in 2000 by the EU and 77 African, Caribbean, and Pacific (ACP) States calls for the establishment of economic partnerships between the EU and regional groupings of ACP members based on reciprocal market access preferences. In order to facilitate the negotiation process and to enhance the development impact of the agreements through increased intra-regional trade, the EU intends the EPAs to be signed with free trade areas or customs unions rather than individual countries. In October 2003, the negotiations were officially launched between the European Union and the Central African country group, which consists of the members of CEMAC plus Sao Tomé and Principe and (since January 2006) the Democratic Republic of Congo.

3.1 Importance of Trade within the Region

According to official statistics, the value of trade (imports plus exports) with other countries in Sub-saharan Africa amounted to about 14 per cent of CAR's total trade during the period from 2003 to 2005. This share is remarkably small for a landlocked country. The latter face additional trade transaction costs related to transit and border clearance when they try to reach maritime ports for inter-continental shipment, so that trade with neighboring countries is relatively more advantageous. Yet, CAR's intra-continental trade share falls far short of the average of landlocked countries in Sub-Saharan Africa, and is, indeed, lower than the average of all countries on the continent (Figure 5).

Figure 5: Share of trade with sub-Saharan countries in total trade
(three year average, 2003-05)



Note: Only those imports and exports are considered for which the partner country is identified.
Source: World Bank staff based on IMF Direction of Trade database.

Two-thirds of CAR's African trade are with the country's CEMAC partners, notably Cameroon and Chad (Table 2). CAR thereby imports much more from CEMAC countries than it exports to them. Of the non-CEMAC members of CEEAC, only DR Congo is of significant importance as a trading partner, and, contrary to its trade relationship within CEMAC, CAR runs a merchandise trade surplus with this neighbor. No trade was reported during 2003-05 with the CEEAC-members Angola, Burundi, Rwanda, and Sao Tomé and Principe.

On a sectoral basis, CAR ran trade deficits with its CEMAC partners in almost all product groups in 2005 (Table 3). The largest net-imports occurred for food and beverages, tobacco, and non-metallic minerals (such as cement). The only products where regional exports from CAR exceeded regional imports were timber and timber-related products. However, official figures on regional trade should be interpreted with care, as they are based on information from the main computerized border stations only. Customs posts in the provinces, which presumably process a proportionally larger share of trade with regional neighbors, are not covered in official statistics.

Table 2: Geographical structure of CAR's merchandise trade within the region
(per cent of total trade)

	Imports			Exports			Total trade		
	2003	2004	2005	2003	2004	2005	2003	2004	2005
Cameroon	13.8	13.0	13.6	0.0	0.0	0.0	6.3	6.9	7.8
Chad	3.2	3.0	3.1	0.3	0.3	0.4	1.6	1.7	2.0
Congo, Republic	1.0	0.1	0.2	0.2	0.1	0.1	0.5	0.1	0.2
Equatorial Guinea	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gabon	0.1	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0
CEMAC	18.0	16.2	17.0	0.4	0.5	0.6	8.5	8.8	10.0
Angola	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Burundi	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Congo, Dem. Rep.	2.3	2.1	2.2	3.0	3.7	4.6	2.6	2.9	3.3
Rwanda	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Sao Tomé and Principe	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
CEEAC	20.3	18.3	19.2	3.4	4.2	5.2	11.1	11.7	13.3
Other Sub-saharan Africa	4.0	3.0	2.9	1.0	0.3	0.4	2.4	1.7	1.8
Total Sub-saharan Africa	24.3	21.3	22.1	4.4	4.4	5.6	13.6	13.4	15.1

Note: Only those imports and exports are considered for which the partner country is identified.
Source: IMF Direction of Trade database.

Moreover, regional trade might be substantially underestimated due to informal cross-border links. These transactions are naturally most important with the countries with which CAR shares borders, i.e. Cameroon, Chad, Sudan, and DR Congo. Some strong traditional trade routes exist with these countries, and the natural conditions permit transactions outside official channels. While by its nature no exact valuation of unofficial cross-border flows is available, the general consensus is that informal activities account for a significant share of total trade within the region.

Over the past years, informality might have lost somewhat in importance, though, as the harmonization of trade policies and regulations between CAR and its neighbors and the phasing out of intra-regional trade barriers within CEMAC has lowered formal trade transactions costs and reduced the incentives to use unofficial channels. Also, the adoption and implementation of a common external tariff has eliminated the gains that could earlier be obtained from world market imports into low protection countries and subsequent informal transshipment into high protection countries.

Table 3: Sectoral structure of CAR's merchandise trade with CEMAC partners, 2005
(Francs CFA)

ISIC-3 Code	Sector	Imports (incl. re-imports)	Exports (incl. re-exports)	Net-Exports
01	Agriculture	202 537 950		- 202 537 950
02	Forestry		1 095 059 287	1 095 059 287
05	Fishing		4 000 000	4 000 000
14	Other mining	166 759 500		- 166 759 500
15	Food & beverages	1 831 264 200	13 641 900	-1 817 622 300
16	Tobacco	1 381 661 000		-1 381 661 000
17	Textiles	293 874 000		- 293 874 000
19	Leather	2 372 500		- 2 372 500
20	Wood products, except furniture	2 980 000	49 987 521	47 007 521
21	Paper products	103 315 400		- 103 315 400
22	Publishing &printing	56 519 550		- 56 519 550
23	Coke & refined petroleum	180 685 100	15 008 900	- 165 676 200
24	Chemical products	538 605 040	7 149 000	- 531 456 040
25	Rubber & plastics	271 207 285	6 000 000	- 265 207 285
26	Non-metallic minerals	1 759 041 800		-1 759 041 800
27	Basic metals	704 852 680		- 704 852 680
28	Fabricated metals	219 376 937	66 225 000	- 153 151 937
29	Machinery & equipment	8 250 000	3 700 100	- 4 549 900
30	Office & computing machinery	650 000		- 650 000
31	Electrical machinery	4 703 300	1 000 000	- 3 703 300
33	Medical & optical instruments	452 900		- 452 900
34	Motor vehicles & trailers	414 713 300		- 414 713 300
35	Other transport equipment	2 270 487		- 2 270 487
36	Furniture	184 309 800	500 000	- 183 809 800
99	Goods not elsewhere specified		1 038 200	1 038 200
	Total trade	8 330 402 729	1 263 309 908	-7 067 092 821

Note: Information based on transactions processed through ASYCUDA, so that trade through non-computerized border stations is not covered.
Source: World Bank staff based on information from National Authorities.

2.2 Status of Regional Integration Initiatives

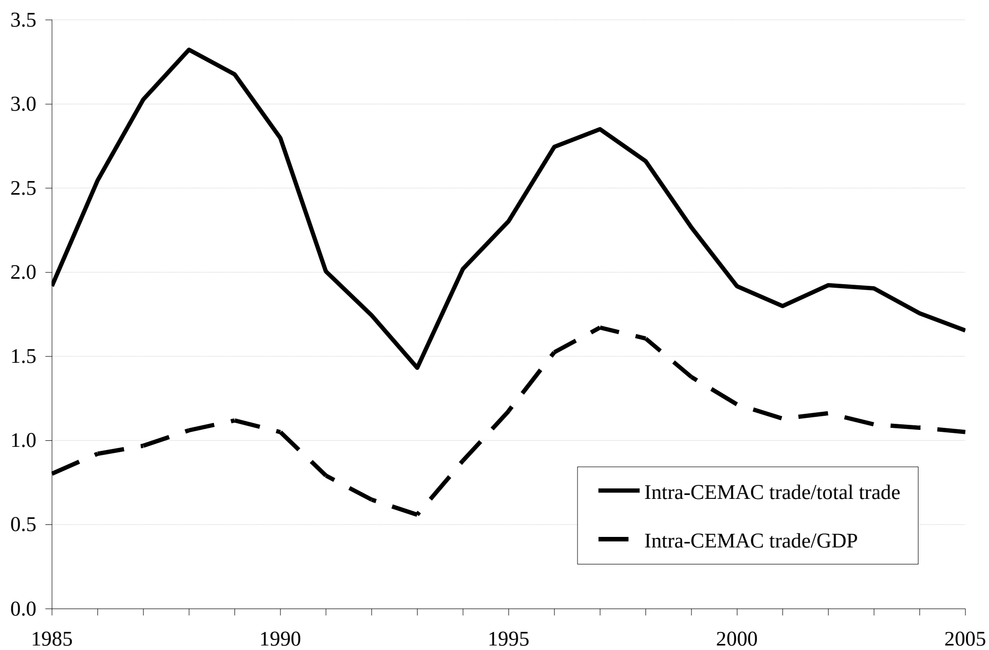
Central Africa has a long history of regional integration. CAR, Chad, Congo, and Gabon first formed the Equatorial Customs Union (UDE, Union Douanière Equatoriale) in 1959, to which Cameroon acceded in 1961. Subsequently, the five countries further intensified economic cooperation in the region, when forming the Customs and Economic Union of Central Africa (UDEAC, Union Douanière et Économique de l'Afrique Centrale) in 1964 and inviting Equatorial Guinea to join the Union in 1983. After the region had endured several economic crisis during the 1980s and early 1990s, renewed impetus for regional integration was sought by signing the Treaty that devised CEMAC as a successor organization of UDEAC in 1994. Member countries ratified the Treaty in 1999 and thereby formally established CEMAC.

The signing of the CEMAC Treaty coincided with a large-scale devaluation of the Francs CFA and the adoption of a common external tariff that all members apply to third country imports. Intra-CEMAC trade was initially subject to a generalized preferential tariff of one-fifth of the CET-rate, but these duties were phased out in 1998. Also, all quantitative restrictions on external and intra-regional trade were converted into tariffs of up to 30 per cent during a transition period, and then eliminated in 2000. In addition to harmonizing tariffs, CEMAC has also established common guidelines on customs valuation, excise taxes, and value-added taxes.

CAR is also a founding member of CEEAC, which was established in 1983 as a wider economic community of Central African states. CEEAC brought together the members of UDEAC, the members of the Economic Community of the Great Lakes States (Burundi, Rwanda, and Zaïre/DR Congo), as well as Sao Tomé and Principe. Angola joined the Community in 1999. One recent objectives of this regional arrangement has been to foster trade integration through preferential tariff treatment of goods originating in member countries. A free trade initiative was supposed to be launched in July 2004 and all intra-regional trade barriers are scheduled to be eliminated by January 2008. However, implementation of the free trade arrangements has been lagging behind the original schedule.

Both CEMAC and CEEAC are multi-faceted arrangements that try to advance integration in several domains. Yet, with respect to the aim of fostering more intensive trade flows, regional integration in Central Africa has had only very modest success so far. Indeed, in relative terms intra-CEMAC imports and exports have declined markedly over the past decade and account now for less than two per cent of total imports and exports, or just over one per cent of member countries' GDP (Figure 6). For most CEMAC members intra-regional trade is only of marginal importance. The exceptions are imports of the two landlocked countries, CAR and Chad, which account for more than 10 per cent of the countries' respective purchases abroad.

Figure 6: Share of intra-CEMAC trade in total trade of CEMAC members
(per cent)



Source: World Bank staff based on IMF Direction of Trade database.

The declining relative importance of intra-regional trade in itself does not imply that CEMAC has failed in its aims, as the reduction in trade between members over time might have been even more pronounced without the arrangement. Instead, careful economic analysis is needed to disentangle the different effects of regional integration and evaluate their overall impact (Box 1). One econometric study used a gravity model and data over the period from 1948 to 2000 to assess different regional trade agreements (RTAs), including CEMAC. The analysis found that the trade impacts of CEMAC have been more modest than those of most other RTAs (Figure 7). Moreover, compared with a "normal" level of trade intensity that would be expected according to the countries' economic size and geographical proximity, the analysis estimates that CEMAC has had a very small, but positive impact on intra-regional trade flows. On the other hand, extra-regional imports and exports are below expectations, suggesting that CEMAC with its high common external tariff might have given rise to harmful trade diversion rather than beneficial trade creation.

Box 1: Welfare impacts of regional integration initiatives

The overall welfare consequence of regional integration depend on several factors. If the reduction of intra-regional trade barriers fosters partner countries to expand output and exports of products for which they are internationally competitive, the price of final goods or production inputs on the importing country market falls to the benefit of consumers and input-purchasing producers. In this case, welfare-enhancing trade is created.

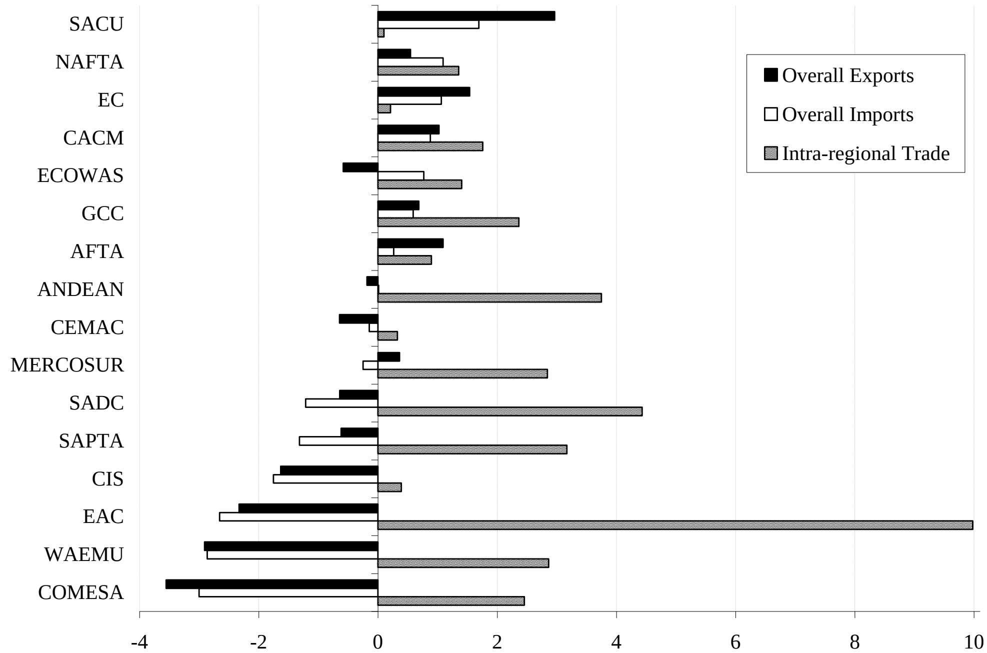
Moreover, regional trade initiatives can have beneficial indirect effects. Opening domestic markets to partner countries, for example, can increase competition in sectors with previously highly concentrated industrial structures and thereby reduce the monopolistic pricing power of incumbents. Such pro-competitive impacts are particularly important for countries like CAR that have only a nascent domestic competition policy. Also, regional cooperation can be effective in harmonizing customs procedures and domestic regulations in services industries. Adopting common rules on investment, for example, has the potential to encourage increased inflows of foreign direct investment (FDI) by enhancing the credibility of FDI-policies and providing a restraint on sudden policy reversals.

Some observers justify RTAs in political economy terms by seeing them as laboratories for international integration, training grounds for negotiations at a broader level, and strategic means of trade policy making. By teaming up with regional partners, countries may be able to increase the weight of their positions in international trade negotiations and possibly achieve more favorable negotiation outcomes. Also, regional trade agreements make it possible for countries to gain some control over the trade policy of their partner countries.

Conversely, engaging in RTAs implies passing parts of a country's sovereignty on to the regional bloc. For example, as a result of joining the EAC customs union, CAR can no longer freely decide on its level of import duties, but depends on consensus with the other CEMAC members to pursue changes to the common external tariff. Hence, the institutional framework for trade policy making changes.

Furthermore, RTAs may result in losses of government revenues, as tariffs on intra-regional trade are phased out, or promote costly trade diversion rather than welfare-enhancing trade creation, if trade is shifted from efficient producers outside the RTA to preferential trading partners that produce at higher costs. In this case, the government loses tariff revenue on imports from third countries, without domestic producers benefiting to a corresponding extent from lower import prices. The risk for trade diversion to occur is particularly high if MFN tariffs remain high and trade with partner countries accounts for only a small share of overall trade (World Bank, 2004). A recent review of studies on the trade and welfare effects of customs unions concluded that the elimination of intra-regional trade barriers between small developing countries is likely to generate mostly trade diversion and little trade creation, unless significant reductions in MFN-tariffs accompany the regional integration efforts (Schiff and Winters, 2003).

Figure 7: Estimated deviation of trade flows from expected levels in different RTAs
(in exponential units)



Source: World Bank (2005).

One issue that could jeopardize the success or regional integration in Central Africa is the overlapping membership of countries in different RTAs. All members of CEMAC are also members of CEEAC. Moreover, some countries that belong to CEEAC are also members of the Common Market of Eastern and Southern Africa (Angola, Burundi, DR Congo, Rwanda) or the Southern African Development Community (Angola and DR Congo). Some observers have argued that countries could maximize the benefits from regional integration by participating in several arrangements simultaneously (Lyakurwa *at al*., 1997). Liberalizing trade within smaller groups facilitates the coordination and harmonization of national policies, and makes it possible to increase competition for sensitive domestic industries at a more measured pace. Multiple agreements also open up alternative liberalization tracks that provide countries with flexibility to switch their integration focus in the event that progress within a particular grouping were to stall. Moreover, since aid agencies frequently provide funds for region-wide projects, participation in multiple regional arrangements might be seen as a means to fully exploit the potential pool of donor-funds.

On the other hand, there are significant drawbacks. Since each of the agreements involves different partners, different rules of origin, different tariff schedules, and different implementation periods, effectively administrating the multiple regional integration efforts can pose major political and technical challenges and increase trade transactions costs. These consequences from overlapping agreements are bound to intensify as many of the existing arrangements, such as CEEAC, are scheduled to deepen their integration by moving from preferential agreements to free trade areas or customs unions.

Multiple membership of overlapping RTAs creates demanding requirements in several respects. In the private sector, traders have to operate within different trade regimes, each with its own tariff rates, regulations and procedures. For example, non-coordination amongst regional arrangements concerning transit bonds has been cited by private sector representatives as a significant impediment. In the border services, customs officials have to deal with different rules of origin, trade documentation, and statistical nomenclatures, thereby multiplying internal procedures and paperwork. And on the political level, negotiating and serving different regional initiatives can absorb large amounts of scarce administrative resources and occupy policymakers' attention to a considerable extent. This concerns, in particular, the preparation, attendance, and follow-up of meetings of technical experts or ministers. At times, integration efforts are duplicated and counterproductive competition between countries and regional institutions – including with respect to dispute resolution – can emerge (UNECA, 2004). In addition, budgetary contributions from member states towards the administration costs of the various RTAs can be a significant burden, as indicated by the arrears in membership contributions of CEMAC members (Performances Management Consulting, 2006).

Potentially conflicting integration schemes as a result of simultaneous participation in several regional trade agreements are another major drawback. Such contradictory requirements indeed have the potential to create serious dilemmas for trade policy makers in CAR and its CEMAC and CEEAC partners. In particular, with CEMAC already a customs union, CEEAC, COMESA, and SADC are also hoping to form free trade areas and subsequently customs union in the medium-term future. Since one country can not realistically apply two different common external tariffs, let alone implement the customs and fiscal integration (e.g. revenue-sharing) that are basic components of fully functioning customs unions, CAR and its RTA partners are sooner or later bound to face the choice about which agreement they want to go with.

One issue that deserves particular attention in the context of overlapping agreements is the potentially significant trade transactions costs that can result from the need to comply with multiple rules of origin (ROO) regulations (Brenton and Imagawa, 2004). Preferential trading agreements use ROOs to ensure that third countries do not unduly benefit from the preferential treatment that members of a RTA grant to one another. They specify the amount of processing that a product must undergo in partner countries in order to quality for market access under the preferential agreement. These rules can add considerable complexity to the trading process and augment the costs of international trade, in particular if the ROOs vary across different agreements.

Moreover, companies not only have to comply with the rules on sufficient domestic processing, but also need to obtain a certificate from the competent authorities that proves compliance. Within North America, the costs of providing appropriate documentation to prove origin have been estimated to amount to as much as 3 per cent of import value (Anson *et al.,* 2005). These costs might well be even higher for small-scale firms in developing countries that do not have sophisticated accounting procedures in place in order to keep track of the geographical origin of their production inputs. If such firms are then confronted with ROOs that vary across different agreements, the effort of showing compliance can become prohibitively expensive.

Strict and complex ROO might also inhibit firms to integrate into global or regional production networks. Indeed, it has been argued that ROO can be trade diverting and can "export" protection from one trading partner, who imposes strict ROO, to another, who adjusts local production patterns accordingly (Krueger, 1997). In particular, producers faced with restrictive ROOs and the prospect of benefiting from preferential tariffs might well turn away from low-cost, third country suppliers of intermediate inputs and towards highly protected, high-cost suppliers located in the partner country, thereby increasing their production costs and making them less competitive in the global market (Krishna and Krueger, 1995).

Multiple origin schemes also place a burden on the administrative capacity of the customs services. A recent world-wide survey of customs agencies in member countries of the

World Customs Organization sought information on the role of customs in issuing and checking certificates of origin and requested the views of customs officials on their experiences of administering ROOs (Brenton and Imagawa, 2004). Almost half of all respondents stated that overlapping agreements with differing ROO created problems, and of the respondents from Africa, more than two-thirds agreed with the statement that overlapping ROO were problematic.

In addition, there are issues of integrity. The existence of different rates of import duty from different countries provides incentives for false invoicing, so as to show origin in the country subject to lower duties. Also, situations at the border may arise that are open to abuse or subject to excessive bureaucracy, thereby inflicting costs on traders in addition and beyond those related to compliance with the applicable ROO regulations.

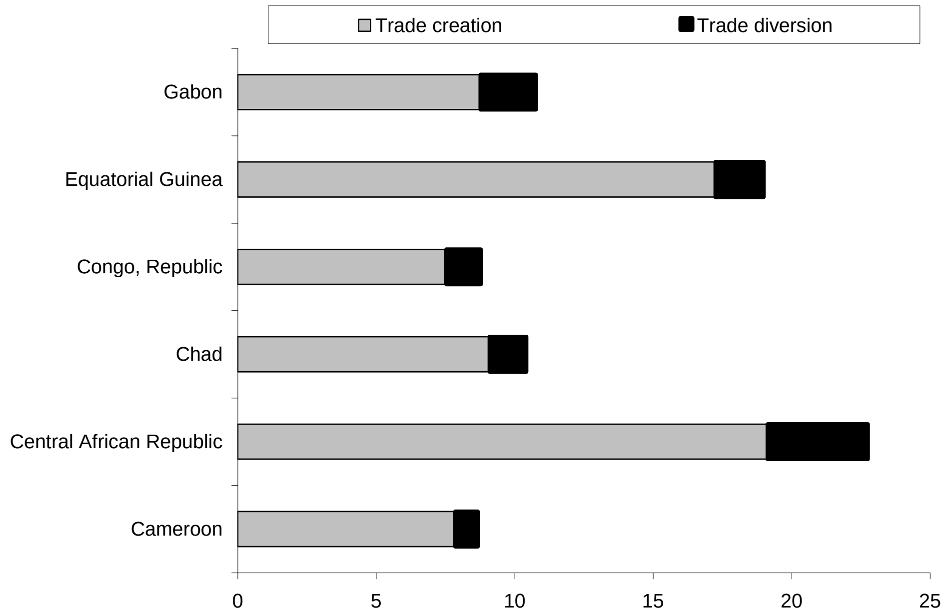
3.3 Negotiations of an Economic Partnership Agreement

The conclusion of the intended Economic Partnership Agreement with the European Union is likely to have major impacts on the regional configuration in Central Africa and the countries in the region. The EPA negotiations started in 2004 and are supposed to conclude by the end of 2007. The prospective EPA agreement will not improve the preference margins that countries like CAR currently enjoy in the EU market. As a least developed country, CAR is eligible for duty and quota free access to the EU market under the EBA initiative, which is of unlimited duration. However, the EBA rules of origin are more restrictive than those under the Cotonou Agreement, notably by not allowing “full” regional cumulation and a lower tolerance threshold for third country content. The Government, therefore, has all the interest in maintaining the existing benefits and might aim in the EPA negotiations to obtain rules of origin provisions that are at least as favorable as those currently enjoyed under Cotonou. And if it were possible to negotiate more favorable specifications that confer origin based, for example, on a simple change of tariff heading or a low value-added rule, additional market access opportunities for CAR’s exporters might open up.

On the imports side, reciprocity means that over a twelve year transition period from 2008 to 2020, CAR would have to open its market to supplies from EU members. This market opening will have the typical effects of preferential trade liberalization, bringing benefits from trade creation, increased competition and lower consumer prices at the expense of costs related to trade diversion and loss of tariff revenue. Partial equilibrium analysis of a prospective EPA in Central Africa finds that imports from the EU would increase by 8-23 per cent and that trade creation would exceed trade diversion for all CEMAC members (UNECA, 2005). The trade effects would be most pronounced for CAR (Figure 8). Moreover, the study estimates that a quarter of the trade diversion in CAR would come at the expense of other CEMAC members, while in the other countries trade diversion would almost exclusively be due to third country imports being replaced by imports from the EU.

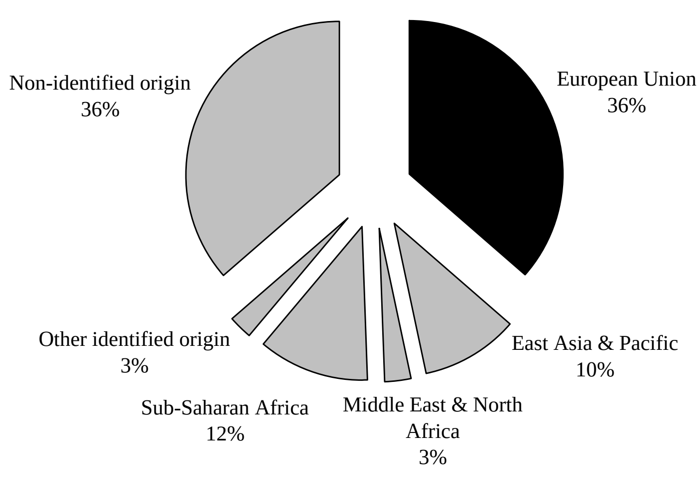
Concerning the impact on government revenues, CAR’s fiscal revenues on imports from EU members accounted for 36 per cent of total revenues collected on imports whose origin was specified in 2005 (Figure 9). In addition, a share of the imports of unspecified origin, which equally accounted for about 36 per cent of the total, might have also come from EU members. Yet, the available information on fiscal revenues raised at the border includes receipts from customs surcharges and indirect taxes, such as excises and VAT, in addition to import duties. Only the latter, which across all imports accounted for a third of 2005-revenues, would be lost as a result of an EPA.

Figure 8: Estimated increase in EU imports as a result of an EPA Agreement
(per cent of total imports in 2005)



Source: UNECA (2005).

Figure 9: Import tax revenue according to origin of imports, 2005



Note: Information based on transactions processed through ASYCUDA, so that trade through non-computerized border stations is not covered. Tax receipts on imports of non-identified origin, which account for 36 per cent of the total, not included.
Source: World Bank staff based on information from National Authorities.

The current share of duties on EU imports represents the lower boundary of the prospective border tax losses following the full implementation of a prospective EPA. Actual duty losses will be higher, as the preferential market access granted to the EU will tend to lead to a replacement of imports from other countries by duty-free EU supplies. Revenue losses will be attenuated to the extent that certain “sensitive” products were to be exempted from the liberalization process.

The coverage of the EPA negotiations is *a priori* not limited to the goods sector, but might also embrace services. This part of the negotiations could provide opportunities for the Government to request EU support for transport and trade facilitation measures that would help reduce CAR’s disadvantages as a landlocked country. The Government might also use the EPA negotiations to lock in and advance reforms of its domestic services sector. Policies that govern international trade in services are typically domestic regulations, some of which serve important policy objectives (for example prudential regulations in the banking sector), so that it is crucial to design and implement regulations properly. Technical assistance could be sought for identifying reform needs in particular services sectors that would bring the regulatory framework into line with international best practice.

4. RECOMMENDATIONS FOR POLICY REFORM AND TECHNICAL ASSISTANCE

The following Table develops and presents a set of policy reform priorities and technical assistance needs that emerges from the preceding discussion.

Table: Policy Reform and Technical Assistance Matrix

Policy issue	Action recommended	Requirements: Implement existing policy	Requirements: Change policy/ legislation	Requirements: Seek technical assistance	Agency involved	Time frame
Domestic trade policy						
	Reduce reliance on tariff revenue by reducing "leakage" and strengthening the tax system.	X	X		GOCAR, MCIPME, MFB	Longer term
	Reduce tariff escalation by pushing for a reduction in the top rate within CEMAC.		X		MCIPME	Longer term
	Review effectiveness of sugar policy with a view to liberalize imports.		X		GOCAR, MCIPME, MFB, MDR	Short-Medium term
Regional integration						
	Use EPA negotiations to obtain more favorable rules of origin for access to the EU market		X		MCIPME	Medium term
	Push for simple, non-restrictive rules of origin specifications in regional agreements.		X		MCIPME	Longer term
	Aim for flexibility within RTAs in order to avoid contradictory requirements.		X		GOCAR, MCIPME, MFB	Longer term
	Pursue deeper regional integration through harmonization of trade standards and behind-the-border regulations.		X		MCIPME	Longer term
	Seek technical assistance for services sector reform to adapt regulations to best practice.			X	MCIPME	Longer term

Note: Agency abbreviations: GOCAR = Government of CAR; MCIPME = Ministry of Commerce, Industry, and Small and Medium Enterprises, MFB = Ministry of Finance and Budget, MDR = Ministry of Rural Development. Time frame: Short term – within 12 months Medium term – within 2 years Longer term – 2 to 5 years.
Source: World Bank Staff.

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